August 05, 2019 at 2:30 pm IST

Q1 FY2020
Earnings Conference Call Transcript

MAIN SPEAKER:
Pratibha K. Advani, Chief Financial Officer

Moderator: Ladies and gentlemen, good day and welcome to the Tata Communications Q1 FY'20 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Vipul Garg – Head of Investor Relations at Tata Communications. Thank you and over to you sir.

Vipul Garg: Good Afternoon, everyone and welcome to Tata Communications earning conference call. We have been joined today by Pratibha Advani -- Chief Financial Officer. The Results for the quarter ended 30th June 2019 were announced on Friday and the 'Quarterly Fact Sheet' is available on our website. I trust you would have had the opportunity to pursue the key highlights. We shall commence today's call with comments from "Pratibha who will share Insights on the Business Progress and Financial." At the end of management's remarks, you will have an opportunity to get your queries addressed.

Before we get started, I would like to remind everyone that some of the statements made or discussed on the conference call today may be forward-looking in nature and must be viewed in conjunction with the risks and uncertainties we face. A detail statement and explanation of these risks are included in our annual filing which you can locate at our website, www.tatacommunications.com. The company does not undertake to update these forward-looking statements publicly.

With that, I would like to turn the call to Pratibha to share her views. Over to you, Pratibha.

Pratibha Advani: Thank you, Vipul. Good afternoon, everyone and thank you for joining us on today's call.

I will commence with some details about organization developments of last quarter that you may already have heard. As you are aware, Vinod has resigned from the position of M.D. and CEO effective 5th July 2019 and has decided to pursue opportunities outside of Tata Communications. Vinod has been with the company for 15-years and has been instrumental in transforming the company into a leading global digital infrastructure provider. We would like to thank and wish Vinod all the best for his future endeavors.

We are pleased to share that Amur S. Lakshminarayanan has been selected to be appointed as the Managing Director and Chief Executive Officer of Tata Communications by the board. Lakshmi, as he is normally called, official appointment confirmation and joining date is subject to the receipt of necessary regulatory approval. We look forward to welcoming Lakshmi to team Tata Communications.

We continue to remain focused to deliver on our strategic roadmap of profitable growth as the global digital infrastructure provider. I would like to share certain trends that are transforming the way enterprises are doing business and use that to underline how we are positioned. Drawing your attention to our Media Services portfolio which has been in the limelight in recent times, having just witnessed the conclusion of the biggest sporting event of the year the ICC World Cup. Traditionally, revenue for sports come from sales of broadcasting rights. But the popularity of on-demand streaming means digitally engaged viewers now expect far more control of how, when and what they want. As a nation, we have not fully tapped the opportunities that digitization offers within sports. We expect the global sports broadcasting and digitization market to touch $31 billion by 2024.

Deeply connected technology such as Augmented Reality or AR, Virtual Reality and IoT, will put fans at the center stage of an immersive experience where there will be frequent interaction between the fans, their teams, their favorite players and their brand sponsors. We see ourselves as enablers of technology and in this instance as an enabler of the technology paradigm itself our solutions are helping sporting bodies, fans and brand owners and businesses, all to benefit from this trend. We are associated with all major sporting events globally and we aim to further strengthen our position through our differentiated offerings.

Another pertinent example that I can share with you is that of connected vehicles, of which we have seen a few introductions in the country quite recently. Vehicle connectivity has become a key topic for all manufacturers and across all geographies.

Our MOVE global mobility platform enables vehicle connectivity across borders. It is designed to provide network independent, cross-border cellular connectivity that carmakers need today to deliver connected car services for both homes and export markets. In a world where devices of phone connected, a single global mobile network enabled by API, automation and the cloud would not only give businesses unprecedented visibility and control overall connected thing wherever they might be but also reduce cost.

Our MOVE platform continues to get excellent traction across industries and we have won a large order from a marquee automobile manufacturer. Recently, we also won a large deal from a global airline. These large deals will provide impetus to our overall revenue growth. In a short span of time we have contracted 164 customers for MOVE platform.

During the quarter, we launched IoT marketplace in India. This offering is intended to bring together different partners including device manufacturers, software developers to start up and system integrators to deploy and manage IoT solutions all under one single platform. This marketplace will enable diverse customers from government, public sector units to enterprises and start-up to choose from a range of offerings and services on a transparent plug-and-play model enabling them to leverage IoT solutions to address the custom requirement.

We have recently operationalized our partnership with Cisco for our SD-WAN solution under the IZO platform. We aim to offer a fully managed hybrid network service that is a fit for digital businesses. It is going to be a resilient cloud-ready network at the service which can grow and scale as needed while ensuring predictable and secure access to data and application. It has been designed to give businesses agility and reduce the complexity of network transformation.

Our IZO suite of offerings provide the solutions that enables to transform legacy connectivity system into a secure, scalable and high performing global network across diverse locations. Through our solutions, an enterprise can get SLAs of a private network along with global reach of internet. IZO had increasingly become important part of Growth Services and is contributing significantly to the overall revenue.

The landscape of doing business continues to evolve with data as the key stone. As a future-ready organization, we too are pursuing digital transformation of our key processes. This is making us more agile and at the same time bolstering our agility to offer on-demand ahead of the curve solutions that can deliver significant benefits to our customers and provides an enhanced user experience.

We have digitized lead to order processes for five connectivity products through our optimist platform. More than 1,000 customers are already using the platform logging in over 1,500 orders.

Before I start about our “Financial Performance”, let me call out some of the changes in financial reporting that has taken place this quarter. Effective April 1, 2019, the company has adopted the new accounting standard IndAS 116 on lease accounting as notified by the government. As per new standard, a lease is considered as a contract that conveys the right to use an asset for a period of time in exchange for consideration. Accordingly, all leases will consist of amortization of right-of-use asset and interest expenses related to lease liability. This has led to a decrease in operating expense and a corresponding increase in depreciation and interest expense and has an impact on reserves and surplus. We have provided a reconciliation statement in our 'Quarterly Fact Sheet'.

Starting on the performance for this quarter, we have started reporting all the metrics in INR except net debt and CAPEX. This will bring consistency and help in easier analysis. Accordingly, we have restated prior period numbers for comparison. Also, for our two subsidiaries, we have started to report numbers net of intercompany eliminations in place instead of standalone numbers in our quarterly fact sheet. This is in line with how we view their performance. Consolidated revenue grew by 5.7% year-on-year and came in at Rs.4,167 crores on the back of strong performance in data business. On QoQ basis, revenue declined by 1.8% primarily due to decline in voice and one-off revenue recognized in Q4 in our Growth Services portfolio. EBITDA for the quarter came in at INR826 crores with a margin of 19.8%. EBITDA grew by 40.7% year-on-year with the margin expansion of 490 basis points over the same quarter last year. On QoQ basis, EBITDA grew by 20.5%. We had a favorable impact of IndAS 116 adoption on EBITDA to the tune of Rs.70 crores. On a like-to-like basis, EBITDA grew by 28.7% YoY driven by strong profitable growth in our Data portfolio. This growth translated to PAT of Rs.77 crores in Q1 as compared to a loss of Rs.199 crores in Q4 which included impairment of our investment in SDC.

Now, moving to our Segment Performance data business witnessed robust growth this quarter despite industry headwinds. Revenue grew by 12.4% YoY which is an industry-leading growth rate and testimony of successful execution of our strategy. Strong growth in both traditional which was up by 6.1% YoY and Growth Services which was up by 29.2% YoY has helped achieve this growth rate.

Our Data revenue for the quarter was Rs.3,278 crores and witnessed a marginal decline of 1.9% QoQ. This decline was due to one-time revenue recorded in Growth Services in last quarter and a significant decline in Innovation Service revenue as we had one-time POC revenue in Q4 from the Innovation product portfolio. EBITDA for the quarter was at INR736 crores witnessing a growth of 42.7% YoY and 25.1% QoQ. Without IndAS 116 impact, EBITDA came in at INR669 crores recording 29.5% YoY growth.

Data Services contribute to 79% of the overall revenue and 89% to overall EBITDA. We have won large deals across our product portfolio which is giving an impetus to our overall revenue growth and profitability.

Now, moving to the Performance within the Data Services portfolio: Traditional Services: This portfolio has been under pressure during FY'19 due to operator consolidation but has now started to stabilize. Revenue for the quarter came in at Rs.2,068 crores witnessing a growth of 6.1% YoY. Within this portfolio, NPL grew by 31.5% and IPL grew by 10.3% YoY. EBITDA came in at Rs.795 crores witnessing a growth of 30.2% YoY and 21.8% QoQ. Margin for the quarter was 38.5%. Without IndAS 116, EBITDA margin would be 36.2%. We have been driving efficiency and productivity in this business to enhance profitability. We have made concentrated efforts towards effective churn management and customer churn is coming down. We have witnessed lowest churn this quarter versus last year which has partially helped in margin improvement and there were one-off cost such as cable repair, etc., in Q4 which have now got normalized in this quarter.

Moving to Growth Services continue to witness strong growth. For the quarter, revenue was Rs.768 crores witnessing a growth of 29.2% YoY on the back of new deal wins and execution of deals in hand. On QoQ basis, revenue declined by 1.5% due to one-time revenue of Rs.25 crores recorded in Q3. This was disclosed in our last earnings call. EBITDA for the quarter was at Rs.21 crores. Within this portfolio, IZO grew by 85%, MMX grew by 71% and Security Services grew by 69% YoY. Other than the above-mentioned products, we have won large deals across MOVE, our global hosted contact center and other services during the last few quarters.

As we start to execute on these deals, we will incur some upfront cost in coming quarters. These services are platform-based and highly customized for each customer, hence requires a longer delivery period which sometimes leads to delay in revenue recognition. We are confident that as we start to deliver the services, we will see higher ramp up in Growth and Innovation Services portfolio.

Coming to our Transformation Services business: Revenue for the quarter came in at Rs.300 crores, translating to YoY growth of 23.4%. New deal wins have helped us to grow this business despite facing challenges. On QoQ basis, revenue has declined by 5.1% because typically in Q4 we get corrective maintenance revenue and this is seasonal in nature. You would recall that we have picked up some low margin deals to showcase our capabilities and this has led to some profitability erosion. EBITDA for the quarter came in at Rs.19 crores with margin coming in at 6.2% due to continued upfront investment in some of these large deals that we are pursuing. Also, with growth coming from existing customers, there is an expectation of higher efficiency from these customers. We have healthy international order book. And as revenue from these deals kick in, we expect profitability to improve in the latter part of the financial year.

Moving to Payment Solutions Business, we continue to rationalize our ATM portfolio with the focus on profitability. In Q1 FY'20, we closed 486 ATMs. Currently, we have a total inventory of 12,399 ATM. We have steadily improved margins by focusing on efficiency and productivity. While revenue grew by 6.2% QoQ, EBITDA grew by 241% QoQ and came in at Rs.19 crores with some benefit coming from IndAS 116. Average transaction per day per white label ATMs have moved to 93 in Q1 versus 88 in Q4. We have witnessed a steady increase in transaction number and our focus is to keep on looking at efficiencies and enhanced profitability.

Moving to the Voice Business, we continue to witness a decline in this portfolio which is in line with industry trends and technology outlook. There was a decline in volume this quarter while the price was largely stable. Revenue for the quarter came in at Rs.890 crores, decline of 1.2% QoQ and 13.3% YoY. EBITDA for the quarter was Rs.89 crores and witnessed a growth of 26.3% YoY and a decline of 7.6% QoQ. We have been able to maintain margin at 10% through temporary benefit of market shift. In long-term we expect the margins to stabilize in the range of 6-7%. CAPEX for the quarter was at USD45 million as compared to USD60 million in Q4 FY'19. CAPEX for Traditional Services was 26 million while for Growth and Innovation we invested 10 million, the balance CAPEX was used towards BAU requirements of the business. Net debt as on 30th June was USD1.248 billion, an increase of 16 million as compared to Q4. This marginal increase was due to salary hike and bonus payout to our employees during the quarter. Our average cost of borrowing for Q1 was 3.93% which has marginally increased by 7 basis points over Q4. In Q1, we generated free cash flow of Rs.315 crores witnessing a growth of 447% over last quarter. This free cash flow is post CAPEX, tax and interest. IndAS 116 impact on reserves and surplus in our balance sheet was Rs.164 crores which has led to decline in our net worth.

To conclude, our strategic focus on offering best-in-class Digital Infrastructure Solutions is showing results. The overall share of profitable Data Services is increasing and performance during the quarter reflects the continued momentum. Robust growth in Enterprise business of a little over 20% and Growth Services of 29% is testimony to the fact that we are now being considered a preferred digital transformation partner. Our Data business has witnessed robust performance both in terms of revenue and profitability. We have a strong order book and we expect this trend to continue as we keep on executing on large deals.

This brings an end to management commentary and I would now request the moderator to open the forum for Q&A. Thank you.

Moderator: Thank you. We will now begin the question-and-answer session. The first question is from the line of Sanjesh Jain from ICICI Securities. Please go ahead.

Sanjesh Jain: One follow up question on the order book. We used to share this order book number. Can you give how does it stand in Q1 FY20?

Pratibha Advani: Sanjesh, while yes, we were sharing the order book, but it is not something that we actually put out in our fact sheet. But our Growth Services order book has grown YoY by 17%; Traditional Services has grown as I recall between1%-2%.

Sanjesh Jain: We mentioned this $1.4 billion in previous call in March in GDS. So, just wanted how does this number look in June?

Pratibha Advani: I think this is still in the same range, Sanjesh.

Sanjesh Jain: One, on the Traditional side. We had a margin of around 36.2% adjusted for IndAS. So, what is the sustainable margin there and was there any one-off gains in this quarter in Traditional Services?

Pratibha Advani: Like I mentioned, the Traditional Services portfolio did get the benefit of IndAS because the rental cost line has now moved from above EBITDA to the depreciation and interest line. This in Traditional as I recall is close to Rs.52-55-odd crores. Our normalized margins I would think would be more in the range of 34-35%.

Sanjesh Jain: So, that is the margin we continue to see because we were earlier guiding of 30%, 31% adjusting for IndAS obviously. So, where do we see this margin now stabilizing?

Pratibha Advani: I would say in the range of 34-35% and of course this quarter as I mentioned in my commentary, we also got a benefit of lower churn. And while the Traditional portfolio looks QoQ to have degrown, but that is primarily because of the FX impact.

Sanjesh Jain: What is FY'20 CAPEX looks like?

Pratibha Advani: That will be more in the range of about 200 million.

Sanjesh Jain: So, lower than what we used to do earlier in the range of 250-275 million, so now this year it looks like 200 million?

Pratibha Advani: Yes, that is right.

Vipul tells me that there are no questions. I guess we have delivered on a strong quarter and all of you are happy with the outcome and the results. On that note, I would like to thank you all once again for joining us on the call and look forward to speaking to you all again in the next quarter. Have a good day. Bye-bye.**Ali Asgar Shakir:** So in FY20 should we go back to the same margin profile that we did in years prior to 2019 or it should take longer?

Moderator: Sure. Thank you very much. On behalf of Tata Communications, that concludes the conference. Thank you for joining us, ladies and gentlemen. You may now disconnect your lines.